

September 15, 2006

MEMORANDUM TO: State Investment Council

FROM: William G. Clark s/*William G. Clark*<sub>(crb)</sub>  
Director

SUBJECT: **Proposed Additional Hedge Fund Investments in  
Archipelago Partners, L.P., AG Super Fund, L.P., and  
OZ Domestic Partners II, Ltd.**

This due diligence memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.12 (a) to report on three proposed direct hedge fund investments: an additional \$85 million commitment to Archipelago Partners, L.P., an additional \$65 million commitment to AG Super Fund, L.P. and an additional \$100 million commitment to OZ Domestic Partners II, Ltd. This will bring the total investment in each fund up to \$150 million.

Please note that these investments will be authorized pursuant to Articles 69 and 100 of the Council's regulations which became effective on June 20, 2005. The investment in Archipelago Partners, L.P., will be considered an Equity Long/Short fund investment as defined under N.J.A.C. 17:16-100.1; the investments in the AG Super Fund, L.P. and OZ Domestic Partners II, Ltd. will be considered Low Volatility fund investments.

The Alternative Investments Procedures adopted by the Council on January 20, 2005 require any potential alternative investment opportunities to be identified and initially evaluated by the Head of Alternative Investments of the Division (myself in an acting capacity) and the applicable Asset Class Consultant (Cliffwater, LLC for direct hedge funds, or "Cliffwater") in coordination with the DOI Investment Committee (Ike Michaels acting as Deputy Director, and myself).

As a result of internal and external sourcing, the DOI Investment Committee identified these proposed investments. Cliffwater and Division staff proceeded to undertake extensive due diligence on these three proposed investments. We

completed the same due diligence process as with all the other alternative investment opportunities presented to the Council.

Based on this due diligence, the Division has determined that each of the proposed investments meets the criteria for investments set forth in the Alternative Investment Procedures.

We are proposing these three investments as additions to our existing investments in the Absolute Return Strategy component of the Alternative Investments program. These funds are well regarded within the institutional investment community, and they are currently willing to accept additional funds from the State of New Jersey. They all have long and very strong performance records which we believe are attributable to a depth of investment talent and strong internal investment processes.

Archipelago Partners, L.P. is an equity long/short fund managed by Wellington Management Corp., one of the largest and most respected institutional investment managers in the world with over \$500 billion in assets under management. This fund utilizes Wellington's proven expertise in fundamental-based equity research and has consistently shown strong returns since inception. The fund is comprised of nine underlying long/short portfolios all managed by senior investment professionals at Wellington. Each portfolio utilizes a unique investment style and/or focuses on particular sectors in the marketplace.

AG Super Fund, L.P. is a multi-strategy fund, managed by Angelo Gordon & Co. Angelo Gordon was founded in 1988 and is a well respected hedge fund and private equity manager. The fund utilizes a bottom-up approach and opportunistically invests in various investment strategies developed by the firm. The firm was formed in 1993, and it has generated strong investment returns throughout its history. While the Fund invests in a variety of investment strategies, it has consistently allocated a significant portion of the portfolio to distressed debt investments and merger arbitrage strategies. Unlike many hedge funds, they also have the expertise to evaluate and source opportunities in relatively illiquid assets such as real estate and private equity.

OZ Domestic Partners II, Ltd. is a multi-strategy fund managed by Och-Ziff Capital Management. OZ is a highly regarded hedge fund manager with \$15 billion in assets under management. The firm has adopted an event-oriented approach within each of their investment strategies, and invests throughout the world. About half of the Fund's current exposure is in Europe and Asia. Since its inception in 1994, the Fund has successfully demonstrated very strong risk-adjusted returns over various market conditions. The founder, Daniel Och, has been and remains very active in all aspects of the operation and has provided consistency to the Fund. He also has been successful in

cultivating a team-oriented culture by expanding the ownership of the Firm to a large number of employees.

A formal written due diligence report for each of the proposed investments was sent to each member of the Investment Policy Committee of the Council on September 8, 2006, and a meeting of the Committee was held on September 13, 2006. In addition to the formal written due diligence reports, all other information obtained by the Division on these three investments was made available to the Investment Policy Committee.

After a review of the extensive due diligence conducted on each fund, the Investment Policy Committee of the Council decided to report on these proposed investments to the full Council pursuant to Step 4 of the Alternative Investments Procedures. Under these procedures, the Council may adopt or otherwise act on this report.

Attached to this memorandum is the SIC Investment Committee's Fund Review Memorandum for the three investments.

We will work with representatives of the Division of Law and outside counsel to review and negotiate specific terms of the legal documents to govern each investment. Since we already have agreements in place with each firm, the additional investments will most likely fall under our existing partnership agreements. In one or more cases, we may determine that it is advantageous for us to invest in a different, but substantially similar, partnership than the entity noted in the memorandum. If this occurs, we will insure that the actual partnership's terms (i.e., fees, liquidity, etc.), are no less favorable than the terms detailed here. In addition, each proposed investment must comply with the Council's "pay to play" regulation (N.J.A.C. 17:16-4). While we are confident that we will work through these issues, the potential exists that a successful resolution will not be reached with one or more of these managers.

We look forward to discussing these proposed absolute return strategy investments at the Council's September 21, 2006 meeting.

WGC:cae  
Attachments